

BITING THE HAND THAT FEEDS YOU? HOTEL BRANDS AND OWNERS IN A POST-COVID-19 WORLD

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The impact of COVID-19 and the measures taken to prevent its spread continues to have a direct and severe effect on global tourism. Hotels and airlines have been impacted disproportionately to their contribution to economic growth and development. The almost complete suspension of international travel for much of 2020 to date and the threat of second waves is having and will continue to have a direct and serious impact on relationships between hotel brands and owners.

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While most brands have been quick to offer capital expenditure holidays and brand standard suspensions as interim and short-term measures, the long-term cost of those measures will inevitably sit with the owners. Operators have been swift to seek ways to raise or preserve funds, for example, through the pre-sale of loyalty points and significant redundancies, which will also impact on the brands in due course. Many owners are naturally focussed on reopening and operating their hotels or resorts. In doing so, it is important to carefully consider the likelihood that COVID-19 will exacerbate and inflame existing issues and disputes between brands and owners. Litigation in relation to the Peninsular Bangkok and JW Marriot Phuket highlights the extent to which these flash points between owners and brands can end up in court and attract public attention, including non-performance, potential conflicts of interest and the impact of loyalty programmes.

As hotels begin to reopen and tourism and travel resumes, brands and owners will be focussed on rebuilding revenue, sales and marketing and cost controls. Alignment without a fair and reasonable agreement on the strategy to deal with these issues between brands and owners, means an already uneasy balance of interests will become more disjointed and divergent than before COVID-19. It is early days and there is still time to identify and implement an approach which recognises both the significant investment of the owners and the need to adopt a more flexible approach to existing and new contracts.

KEY FLASH POINTS BETWEEN HOTEL OWNERS AND BRANDS

Brand management and performance: Management, franchise and other similar agreements are likely to come under close scrutiny as part of plans to revive demand and increase average rates, revenue per available room (RevPAR) and occupancy.

Owners are likely to look more critically at the benefits of the brand and the extent to which retaining the brand, its operating structure and objectives and remaining with the brand will assist in achieving higher average rates, RevPAR and occupancy. This is particularly the case where owner strategies and plans involve levels of flexibility and new or different pricing and service structures, levels and offerings which require brand approval or would not otherwise be consistent with brand pricing and service structures, levels and offerings. Brands which are no longer seen by owners to deliver satisfactory rates, RevPAR and occupancy are likely to be amongst the first targets for owners.

Conflicts of interest: The significant expansion of hotel chains and affiliated brands has had a significant impact on the hotel sector across the Asia-Pacific region. Thailand is no exception to this and, in many ways, exemplifies the issues and flash points for brands and hotels. Across the country, hotels which were previously under separate management agreements and brands that competed for business on this basis now find themselves within the same hotel alliance and using the same loyalty programmes. This has complicated the ability of individual hotels and their owners to brand and market themselves, particularly vis-à-vis their former local competitors. Although consumers now have a greater choice within the same hotel alliance and loyalty programme, it is questionable whether this benefit outweighs the negative impact on hotel branding and marketing.

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Global plans versus local focus and issues: A key issue is the extent to which a hotel fits within the expansion and development plans of the brand. Where the focus of the brand is on expansion and having as many of its hotel brands in one location as possible, this is likely to result in a conflict of interest between the brand and its expansion, and owners and their focus on promoting their individual hotel/s. A balance between the brand's global plans and those of a local owner may be even more challenging to strike in the current environment. The tension between global and local plans and objectives may only serve to highlight issues and flash points in management and other agreements between brands and owners. Headcount reductions at brand regional and global offices may make it more difficult for owners to ensure that they get a fair hearing and for brands to devote the resources to responding to owner requests, proposals and disputes.

Loyalty programmes: Before COVID-19, there were already issues in relation to the costs to owners of brand loyalty programmes. This was particularly so for the larger brands and their loyalty programmes where brand loyalty is focussed on said programme rather than the hotel brands themselves. Owners are faced with little choice but to accept redemption bookings, which can result in high volumes of redemption bookings at low RevPAR and profitability. Owners seeking to rebuild demand and increase average rates, RevPAR and occupancy, may well prefer to focus on revenue rather than redemption bookings in the short to medium-term but are likely to be constrained in their ability to do so by management agreements which require a minimum number of rooms per night to be available for redemptions and the low room rates for redemption bookings. A key issue will be whether these low redemption room rates can be offset by higher per person or per night spend on F&B and other ancillary hotel revenue sources. There is a risk that points sold wholesale to boost the resilience of a brand will result in other costs necessary to accommodate the loyalty scheme offers, such as room upgrades, club or lounge access, early check in and late check out.

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Brands are more likely to critically assess the extent to which a hotel fits within brand messaging and identity. Where a brand or hotel group has multiple hotels in the same location, the current economic environment may make brands more willing to end management agreements with hotels which are not performing or do not meet their requirements, particularly in relation to brand messaging, identity, pricing and service structures, levels and offerings.

Law and forum: Management and other agreements between brands and owners will typically contain an arbitration clause. The scope of the arbitration clause will play a critical and central role in how disputes between owners and brands are resolved. The broader the scope of the arbitration clause, the more difficult it will be for a party to avoid the operation of the clause and seek redress in the courts. An ambiguously or vaguely worded arbitration clause may allow an owner to

commence court proceedings on the basis that the brand would then need to challenge the validity of these proceedings in open court. Even where such a challenge is likely to be successful, owners may file such proceedings to ensure that their dispute with the brand becomes more widely known and publicised to provide an owner with a better negotiating position with the brand.

In challenging such proceedings, brands would need to then assess the prospects of a successful challenge against the consequences of court proceedings, particularly the risk of such proceedings becoming public knowledge. Brands will need to balance the prospects of a successful challenge with the risk that other owners may file similar claims against a brand arising from comparable disputes. By contrast, arbitration allows for any dispute to be dealt with confidentially.

Some brands require owners to accept their choice of applicable law and the forum for an arbitration of any disputes. The extent to which owners can vary these terms depends on their relationship with and importance to the brand and their negotiating position and possibly the support of funders of owners to the owner's approach to its brand. Although the forum should not provide either party with any advantage, the forum of any arbitration will often not be in the same jurisdiction as the owner's hotels. The judgments of local and national courts are not as readily accepted or enforceable as arbitral awards. The outcome of an arbitration will provide the successful owners or brands with an award which can be enforced against assets in a number of jurisdictions.

The choice and qualifications of the arbitrator/s will usually play a more significant role in achieving a neutral arbitration than the choice of law and forum. Owners and brands should consider the following issues in relation to the choice of arbitrator/s:

- Will the dispute be heard by single arbitrator or by a panel of arbitrators?
- To what extent does the arbitration clause define the experience and expertise required of arbitrator/s?
- To what extent must arbitrators have industry experience rather than legal qualifications and experience?

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- Do the language and applicable law reduce or increase the number of potential arbitrators? and
- If the parties cannot agree on the appointment of arbitrators, is the deadlock procedure fair and neutral?

DISPUTE RESOLUTION: STRATEGIES AND OPTIONS

Issues in dispute between brands and owners are neither new nor unusual. The impact of issues in dispute is often determined by how the parties deal with and seek to resolve the issues, including whether to mediate, arbitrate or litigate disputes. The extent to which the issues in dispute are dealt with publicly can be a more significant factor than the cost and duration of steps to resolve the issues in dispute. This is particularly where public discussion and analysis of the issues in dispute may provide one party with a stronger negotiating position or where this may lead to further similar claims.

In assessing how best to proceed, these are issues which should be considered:

- Identify the issues in dispute;
- What are the best- and worst-case scenarios for method/s of dispute resolution?
- Is the dispute about the objective or the strategy to achieve a common objective?
- What are the dispute resolution options available: negotiation, mediation, arbitration, litigation?
- Will a mediation allow the parties to discuss the issues and break any deadlock?
- What can be won and lost in a mediation?
- Can litigation/arbitration resolve the issues or is this a way to get the parties to better or worse negotiating positions?
- Will the litigation/arbitration remain confidential?
- If not, what are the consequences of the dispute being dealt with in the glare of publicity?
- Will resolution of a dispute between brand and an owner open the floodgates? and
- Are brand identity and standards more important to a brand than an owner?

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